

AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name Bay-Arenac Behavioral Health Authority	County Bay
Audit Date 9/30/06	Opinion Date 2/18/06	Date Accountant Report Submitted to State: 3/21/06	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.


We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable boxes for each item below.

- ☐ yes ☒ no 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ yes ☒ no 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☒ yes ☐ no 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ yes ☒ no 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ yes ☒ no 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL: 129/91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ yes ☒ no 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ yes ☒ no 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ yes ☒ no 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ yes ☒ no 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Reports on individual federal financial assistance programs (program audits).	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Single Audit Reports (ASLGU).	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Certified Public Accountant (Firm Name) Yeo & Yeo, P.C. CPAs			
Street Address 3023 Davenport	City Saginaw	State Michigan	ZIP 48602
Accountant Signature 			

BAY-ARENAC BEHAVIORAL HEALTH

Bay City, Michigan

Annual Financial Statements,

Auditors' Report

and Single Audit

September 30, 2005

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3023 Davenport
Saginaw, MI 48602
Phone (989) 793-9830 / (800) 968-0010
Fax (989) 793-0186

Independent Auditors' Report

Bay-Arenac Behavioral Health
Bay City, Michigan

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Bay-Arenac Behavioral Health as of and for the year ended September 30, 2005, which collectively comprise the Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Bay-Arenac Behavioral Health's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Bay-Arenac Behavioral Health as of September 30, 2005 and the respective changes in financial position for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 18, 2006, on our consideration of Bay-Arenac Behavioral Health's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Governmental Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis and budgetary comparison information identified in the table of contents are not a required part of the basic financial statements but are supplemental information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplemental information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Bay-Arenac Behavioral Health's basic financial statements. The accompanying Substance Abuse Prevention and Treatment Schedules identified in the table of contents are presented for purposes of additional analysis as required by the Michigan Department of Community Health, and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Bay-Arenac Behavioral Health's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Bay-Arenac Behavioral Health's basic financial statements. The accompanying other supplemental information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Yeo & Yeo, P.C.

Saginaw, Michigan
February 18, 2006

BAY-ARENAC BEHAVIORAL HEALTH

Management's Discussion and Analysis

For the year ended September 30, 2005

This section of the Bay-Arenac Behavioral Health (the Authority) annual financial report presents management's discussion and analysis of financial performance for the year ended September 30, 2005. This discussion and analysis is designed to assist the reader in focusing on significant financial issues and activities, and to identify significant changes in financial position and results of operations. Please read this section in conjunction with the auditor's report and with our financial statements, notes to financial statements and supplemental information taken as a whole.

The Authority is a Prepaid Inpatient Health Plan (PIHP) for a region consisting of Arenac, Bay, Huron, Montcalm, Shiawassee and Tuscola counties. The Authority subcontracts for Medicaid services and supports with affiliated community mental health services programs (its Affiliates), including Huron Behavioral Health, the Montcalm Center for Behavioral Health, Shiawassee County Community Mental Health Authority and Tuscola Behavioral Health Systems.

State General Fund revenue and other grants and earned contracts continue to be sourced directly from the state and are exclusively related to Arenac and Bay counties. Additionally, the Authority is the designated regional substance abuse coordinating agency, operating as Riverhaven Coordinating Agency, a division of the Authority. The Authority receives Medicaid, state block grant, other federal and state grants and local funding for the provision of substance abuse services in Arenac, Bay, Huron, Montcalm, Shiawassee and Tuscola counties.

OVERVIEW OF FINANCIAL STATEMENTS

Basic financial statements, in accordance with generally accepted accounting principles (GAAP) according to GASB 34, require the presentation of two types of financial statements. These are authority-wide financial statements and fund financial statements.

Authority-wide financial statements include the statement of net assets and the statement of activities. These provide both long-term and short-term information, and present a broad view of the overall financial status in a manner similar to a private sector business. Information presented in these statements is on the accrual basis of accounting. Long-term assets are capitalized and depreciated. Long-term debt is recorded as a liability. Revenues are recorded when "earned" and expenses recorded when "incurred", without regard to the timing of cash receipts or disbursement.

The statement of net assets includes all assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of improving or deteriorating financial position. The statement of activities presents information showing how net assets changed during the year as a result of operating activity.

Fund financial statements contain individual groups of related accounts and are used to report current assets, current liabilities, fund balance, revenues and expenditures for specific activities or funds segregated for legal requirements or other governmental objectives. These are presented in more detail as compared to the authority-wide statements. The fund financial statements are reported on the modified accrual basis of accounting. Only those assets that are "measurable" and "currently available" are reported. Liabilities are recognized only to the extent that they are normally expected to be paid with current financial resources. Purchased capital assets are reported as expenditures in the year of acquisition. Issuance of debt is recorded as a financial resource with current year payment of principal and interest recorded as expenditures.

BAY-ARENAC BEHAVIORAL HEALTH

Management's Discussion and Analysis

For the year ended September 30, 2005

Fund financial statements are divided into two categories. These are governmental fund financial statements and proprietary fund financial statements.

Governmental fund financial statements show how the community mental health supports and services programs were financed in the short term as well as what remains for future spending.

Proprietary fund financial statements show internal service funds reserved for risk management. These funds are held as a self-funded insurance risk reserve to protect against unanticipated current and future financial exposures related to specialty supports and services at-risk contracts.

SUMMARY OF NET ASSETS

The following summarizes the assets, liabilities and net assets on an authority-wide basis as of September 30, 2005 and 2004.

Summary of Net Assets

As of September 30, 2005 and 2004

(In \$000s)

	<u>2005</u>	<u>2004</u>
<u>Assets</u>		
Current assets	\$ 10,375	\$ 7,032
Restricted assets	6,036	6,625
Capital assets	<u>886</u>	<u>835</u>
Total assets	<u>17,297</u>	<u>14,492</u>
<u>Liabilities</u>		
Current liabilities	6,141	4,805
Noncurrent liabilities	<u>1,427</u>	<u>1,235</u>
Total liabilities	<u>7,568</u>	<u>6,040</u>
<u>Net Assets</u>		
Investment in capital assets	886	835
Restricted for capital purposes	292	824
Restricted for risk management	4,515	4,467
Restricted for community reinvestment	1,850	631
Restricted for substance abuse services	398	425
Unrestricted	<u>1,788</u>	<u>1,270</u>
Total net assets	<u>\$ 9,729</u>	<u>\$ 8,452</u>

Current financial position is defined as the excess of current assets over current liabilities. When current assets exceed current liabilities this is an indicator of financial strength and an increase in current financial position is an indicator of improving financial position.

BAY-ARENAC BEHAVIORAL HEALTH

Management's Discussion and Analysis

For the year ended September 30, 2005

The current financial position (excess of current assets over current liabilities) was a positive \$4.2 million, an increase of \$2.0 million or 91.7%, compared to prior year.

Current assets consist of cash and investments, accounts receivable, amounts due from others and prepaid expenses. These are available for current operations and to pay current obligations. Current liabilities include accounts payable, accrued payroll, related taxes and benefits, amounts due to others and deferred revenue.

Restricted assets consist of cash, investments and accrued interest receivable. These assets are restricted for payment of compensated absences, restricted for capital purposes (funded depreciation), and restricted for risk management. Restricted assets of \$6.0 million have decreased by \$589 thousand or 8.9%.

Assets restricted for capital purposes (funded depreciation) was established in fiscal 2003. Annual funding of this account is not to exceed the amount of depreciation expense and the maximum amount of this account is not to exceed the total of accumulated depreciation on capital assets. For fiscal 2005, the Authority fully funded its annual depreciation expense of \$185 thousand, which represents depreciation expense on assets purchased after October 1, 2002.

At year end, the Medicaid risk reserve balance was \$4.5 million and is fully funded to its contractual maximum annual risk exposure of 7.5% of the funds at risk. At year-end, the balance in the state general fund (formula funds) risk management account was \$53 thousand and is not fully funded to its contractual maximum annual risk exposure of 7.5% of the funds at risk.

Capital assets consist of property and equipment having an estimated useful life of more than one year. In fiscal 2005, \$361 thousand was expended for capital acquisitions. Depreciation expense on previously existing and newly acquired capital assets was \$310 thousand (\$125 thousand representing depreciation on assets purchased prior to October 1, 2002 and \$185 thousand representing depreciation on asset purchased October 1, 2002 and later). The net change in capital assets was an increase of \$51 thousand for the year. When capital expenditures exceed depreciation expense, the net increase represents an investment or expansion of capital resources. Conversely, a net decrease represents a reduction in capital resources available for the future.

As of year-end, the net book value of capital assets was 19.7% of the original book value, compared to 20.2% at the end of the prior year. This percentage is a measure of the relative age of property and equipment. If property and equipment is relatively new, this percentage will be high. Conversely, if the percentage is low, it means that property and equipment is relatively old.

Noncurrent liabilities consist of the liability for compensated absences. These include vested earned time off (vacation and sick) pay obligations.

Restricted net assets include investment in capital assets, net of related debt, and amounts restricted for capital purposes (funded depreciation) and for risk management. These were discussed above.

BAY-ARENAC BEHAVIORAL HEALTH

Management's Discussion and Analysis

For the year ended September 30, 2005

Also included in this category is \$1.9 million of unspent Medicaid funds restricted for community investment (for mental health and developmental disability) and \$398 thousand unspent liquor tax proceeds restricted for substance abuse services in their county of origin. These may be spent next year in accordance with their respective restrictions and provisions.

Unrestricted net assets at the end of the year were \$1.8 million, an increase of \$518 thousand or 40.8% for the year. Unrestricted net assets were 11.0% of total assets, up from 9.0% from the prior year.

SUMMARY OF ACTIVITIES

The following summarizes the revenue, expenses and change in net assets on an authority-wide basis for the years ended September 30, 2005 and 2004.

Summary of Activities

For the years ended September 30, 2005 and 2004

(In \$000s)

	<u>2005</u>	<u>2004</u>
<u>REVENUE</u>		
Medicaid specialty supports and services		
Arenac and Bay counties	\$ 26,519	\$ 24,043
Counties under Affiliate subcontracts	32,100	30,511
Regional Substance Abuse	881	858
Prior year support	1,112	-
State general fund priority populations	4,020	4,582
Adults Benefit Waiver	466	-
State substance abuse block grants	1,922	1,932
Program service revenue	103	220
Grants and earned contracts	3,261	3,151
County appropriation	723	671
Affiliate local funds contributions	710	710
Liquor tax revenue	512	490
Interest income	360	128
Other local income	54	48
TOTAL REVENUE	<u>72,743</u>	<u>67,344</u>
<u>EXPENSE</u>		
Personnel expense	13,504	12,271
Operating expense	24,296	22,514
Affiliate subcontract expense	32,100	30,065
Local funds contributed to State	1,255	1,255
Depreciation	310	383
TOTAL EXPENSE	<u>71,465</u>	<u>66,488</u>
CHANGE IN NET ASSETS	<u>\$ 1,278</u>	<u>\$ 856</u>

Excess of revenue over expenses from activities for the current year was \$1.3 million or 1.8% of revenue.

BAY-ARENAC BEHAVIORAL HEALTH

Management's Discussion and Analysis

For the year ended September 30, 2005

Revenue for the year was \$72.7 million, an increase of \$5.4 million or 8.0% from the prior year.

Medicaid specialty supports and services revenue of \$60.6 million represents 83.3% of total revenue and increased \$5.2 million or 9.4% compared to the prior year.

State general fund priority population revenue (formula funding) of \$4.5 million represents 6.2% of total revenue and decreased \$96 thousand or 2.1% compared to the prior year. This funding is established by MDCH as a part of the legislative appropriation process under the Michigan Mental Health Code and is used to provide supports and services to indigent priority populations, including state facility utilization and other allowable expenses. Current year revenue includes \$34 thousand of prior year deferred revenue. There was no lapse of state general funds to MDCH in the current year nor was there a carryforward of state general funds.

Program service revenue of \$103 thousand includes charges for services for consumers not covered by Medicaid risk contracts or state general fund revenue sources. These represent .1% of total revenue and have decreased \$117 thousand or 53.2% over the prior year.

Grants and earned contract revenue of \$3.3 million includes revenue sources for which the use of funds is restricted to a specific purpose. These represent 4.6% of total revenue and have increased \$110 thousand or 3.5% over the prior year.

County appropriation revenue, interest income and other local income are available to meet state matching fund requirements. These revenue sources constitute 1.6% of revenue and have increased \$290 thousand or 34.2% over the prior year.

Total expense of \$71.5 million has increased \$5 million or 7.4% compared to the prior year.

Personnel expense of \$13.5 million is 18.9% of total expense and has increased \$1.2 million or 10.0%.

Operating expense of 24.3 million is 34.0% of total expense and has increased \$1.8 million or 7.9%.

FUTURE OUTLOOK

The state of Michigan continues to struggle in efforts to balance huge budget deficits. Federal deficits are placing additional pressures on Medicaid funding. The effect of these on future funding for community mental health and specialty supports and services is unknown.

Management expects revenues to be flat at best. Support and service demand is expected to increase together with inflationary cost pressures. While the financial position of the Authority is currently healthy, the economic environment will continue to put pressure on the Authority's ability to meet the service and support needs of its constituents.

* * * * *

As always, questions, comments and suggestions are welcomed from interested parties and the general public. These can be directed to management.

Bay-Arenac Behavioral Health
Statement of Net Assets
September 30, 2005

	<u>Governmental Activities</u>
Assets	
Current Assets	
Cash and cash equivalents	\$ 8,481,844
Accounts receivable, net	358,766
Interest receivable	125,492
Due from other governmental units	1,092,089
Prepaid items	<u>317,476</u>
Total current assets	<u>10,375,667</u>
Noncurrent assets	
Cash and cash equivalents-restricted	6,035,753
Capital assets - depreciable, net	<u>886,021</u>
Total noncurrent assets	<u>6,921,774</u>
Total assets	<u>17,297,441</u>
Liabilities	
Current liabilities	
Accounts payable	3,771,061
Accrued wages and other payroll liabilities	391,421
Due to other governmental units	<u>1,979,027</u>
Total current liabilities	<u>6,141,509</u>
Noncurrent liabilities	
Compensated absences	<u>1,426,500</u>
Total liabilities	<u>7,568,009</u>
Net assets	
Invested in capital assets	886,021
Restricted for capital purposes	291,848
Restricted for community investment	1,849,756
Restricted for risk management	4,515,266
Restricted for substance abuse services	398,409
Unrestricted	<u>1,788,132</u>
Total net assets	<u><u>\$ 9,729,432</u></u>

The Notes to the Financial Statements are an integral part of this statement.

Bay-Arenac Behavioral Health
Statement of Activities
Year Ended September 30, 2005

Functions		Program Revenues		Net (Expense) Revenue and Changes Net Assets
		Charges for Services	Operating Grants and Contributions	
	<u>Expenses</u>			
Governmental activities				
Health & Welfare - Mental Health	<u>\$ 71,464,721</u>	<u>\$ 63,553,157</u>	<u>\$ 6,775,095</u>	\$ (1,136,469)
General revenues				
Grants and contributions not restricted to specific programs				2,000,250
Unrestricted investment earnings				239,777
Restricted investment earnings				119,555
Miscellaneous revenues				<u>54,428</u>
Total general revenues and contributions				<u>2,414,010</u>
Change in net assets				1,277,541
Net assets - beginning of year				<u>8,451,891</u>
Net assets - end of year				<u>\$ 9,729,432</u>

The Notes to the Financial Statements are an integral part of this statement.

Bay-Arenac Behavioral Health
Governmental Funds
Balance Sheet
September 30, 2005

	General Fund
Assets	
Cash and cash equivalents	\$ 8,481,844
Accounts receivable, net	358,766
Interest receivable	94,457
Due from other governmental units	1,092,089
Prepaid items	317,476
Cash and cash equivalents - restricted	<u>1,551,522</u>
 Total assets	 <u><u>\$ 11,896,154</u></u>
Liabilities	
Accounts payable	\$ 3,771,061
Accrued wages and other payroll liabilities	391,421
Due to other governmental units	<u>1,979,027</u>
 Total liabilities	 <u><u>6,141,509</u></u>
Fund balances	
Reserved for capital purposes	291,848
Reserved for community investment	1,849,756
Reserved for compensated absences	1,426,500
Reserved for substance abuse	398,409
Unreserved	<u>1,788,132</u>
 Total fund balances	 <u><u>5,754,645</u></u>
 Total liabilities and fund balances	 <u><u>\$ 11,896,154</u></u>

The Notes to the Financial Statements are an integral part of this statement.

Bay-Arenac Behavioral Health
Reconciliation of the Balance Sheet of Governmental Funds
to the Statement of Net Assets
September 30, 2005

Total fund balance - governmental funds	\$ 5,754,645
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.	
Add: capital assets	4,500,275
Deduct: accumulated depreciation	(3,614,254)
An internal service fund is used by management to cover the risk of overspending the Managed Care Specialty Services Program contract. The assets and liabilities of the internal service fund are included in governmental activities in the statement of net assets.	
Add: net assets of governmental activities accounted for in the internal service fund	4,515,266
Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:	
Deduct: compensated absences	<u>(1,426,500)</u>
Net assets of governmental activities	<u><u>\$ 9,729,432</u></u>

Bay-Arenac Behavioral Health
Governmental Funds
Statement of Revenues, Expenditures and Changes in Fund Balances
Year Ended September 30, 2005

Revenues

State grants	
State General Fund - DCH Contract	\$ 4,019,912
Adults Benefit Waiver - DCH Contract	465,960
Substance abuse	1,922,271
Title XX	21,320
Other state revenues	<u>90,582</u>
Total state grants	<u>6,520,045</u>
Federal and State grants	<u>310,184</u>
Contributions - local units	
County appropriations	722,679
Affiliate contributions	710,280
PA 2 liquor tax	<u>512,156</u>
Total contributions - local units	<u>1,945,115</u>
Charges for services	
Medicaid - DCH contract	59,499,819
Medicaid - other	102,784
Medicaid - prior year settlement	1,112,003
Client and third party pay	56,541
Other earned contract revenue	<u>2,782,010</u>
Total charges for services	<u>63,553,157</u>
Interest and rents	
Interest	<u>239,777</u>
Other revenue	<u>54,428</u>
Total revenues	<u>72,622,706</u>

The Notes to the Financial Statements are an integral part of this statement.

Bay-Arenac Behavioral Health
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
Year Ended September 30, 2005

Expenditures

Health & Welfare - Mental Health

Current

Personnel costs \$ 13,312,859

Operating expenditures 57,649,960

Capital outlay 361,324

Total expenditures 71,324,143

Revenues over (under) expenditures 1,298,563

Other financing sources (uses)

Transfers from internal service fund 71,349

Net change in fund balance 1,369,912

Fund balance, beginning of year 4,384,733

Fund balance, end of year \$ 5,754,645

Bay-Arenac Behavioral Health
Reconciliation of the Statement of Revenues, Expenditures and Changes
in Fund Balances of Governmental Funds
to the Statement of Activities
Year Ended September 30, 2005

Net change in fund balances - total governmental funds	\$ 1,369,912
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Amounts reported for governmental activities in the statement of activities are different because:

Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense.

Add: capital outlay	361,324
Deduct: depreciation expense	(310,485)

An internal service fund is used by management to cover the risk of overspending the Managed Care Specialty Services Program contract. The net revenue (expense) of the fund attributable to those funds is reported with governmental activities.

Add: interest income from governmental internal service funds	119,555
Add: transfers from General Fund	(71,349)

Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the funds.

Less: increase in accrual for compensated absences	<u>(191,416)</u>
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Change in net assets of governmental activities	<u><u>\$ 1,277,541</u></u>
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Bay-Arenac Behavioral Health
Proprietary Fund
Statement of Revenues, Expenses and Changes in Fund Net Assets
Year Ended September 30, 2005

	Governmental Activities Internal <u>Service Funds</u>
Non-operating revenues (expense)	
Interest income	\$ 119,555
Transfer to General Fund	<u>(71,349)</u>
Change in net assets	48,206
Net assets, beginning of year	<u>4,467,060</u>
Net assets, end of year	<u><u>\$ 4,515,266</u></u>

The Notes to the Financial Statements are an integral part of this statement.

Bay-Arenac Behavioral Health
Proprietary Fund
Statement of Cash Flows
Year Ended September 30, 2005

Governmental
Activities
Internal
Service Funds

Cash flows from noncapital financing activities

Transfer from General Fund	\$ (71,349)
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Cash flows from investing activities

Interest Income	<u>88,520</u>
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Net increase in cash and cash equivalents	17,171
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Cash and cash equivalents, beginning of year	<u>4,467,060</u>
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Cash and cash equivalents, end of year	<u><u>\$ 4,484,231</u></u>
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Bay-Arenac Behavioral Health
Notes to Financial Statements
September 30, 2005

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements of Bay-Arenac Behavioral Health have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). The following is a summary of the Authority's significant accounting policies:

Reporting Entity

The Authority operates under the provisions of Act 258 - Public Acts of 1974 (the Michigan Mental Health Code), as amended. The Authority arranges for or provides supports and services for persons with developmental disability, adults with severe mental illness, children with serious emotional disturbance. These supports and services are made available to residents of Arenac and Bay counties who meet eligibility and other criteria. As the community mental health services program for Arenac and Bay counties, the Authority also serves to represent community members, assuring local access, organizing and integrating the provision of services, coordinating care, implementing public policy, ensuring interagency collaboration, and preserving the public interest.

The Authority was designated by the Michigan Department of Community Health as the Medicaid Prepaid Inpatient Health Plan (PIHP) for its affiliation regional service area including Arenac, Bay, Huron, Montcalm, Shiawassee and Tuscola counties. The Authority arranges for or provides supports and services for Medicaid-eligible persons with developmental disability, adults with severe mental illness, children with serious emotional disturbance, and individuals with addictive disorder and substance abuse. To fulfill its obligation under this designation, the Authority subcontracts with its other community mental health services program affiliates, specifically:

- Huron Behavioral Health,
- Montcalm Center for Behavioral Health
- Shiawassee County Community Mental Health Agency, and
- Tuscola Behavioral Health Systems

Further, the Authority was designated by the Michigan Department of Community Health as the substance abuse coordinating agency operating as Riverhaven Coordinating Agency, a division of the Authority. The regional coordinating agency has responsibility for a service area that includes Arenac, Bay, Huron, Montcalm, Shiawassee and Tuscola counties. The Authority arranges supports and services for individuals with addictive disorder and substance abuse who meet eligibility and other criteria. To fulfill its obligation under this designation, the Authority subcontracts with a network of substance abuse providers.

In accordance with accounting principles generally accepted in the United States of America and GASB Statement 14 *The Financial Reporting Entity*, these financial statements present all of the Authority's funds. The criteria established by the GASB for determining the reporting entity include oversight responsibility, fiscal dependency, and whether the financial statements would be misleading if data were not included. The Authority has no component units.

Government-wide Financial Statements

The government-wide financial statements (i.e. the statement of net assets and the statement of activities) report information on all of the activities of the Authority. Governmental activities are normally supported by intergovernmental revenues.

Bay-Arenac Behavioral Health

Notes to Financial Statements

September 30, 2005

The statement of activities demonstrates the degree to which the direct expenses of a function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include charges to consumers who purchase, use or directly benefit from services provided by a given function. Program revenues also include grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Other items not properly included among program revenues are reported instead as general revenues. Resources that are dedicated internally are reported as general revenues rather than as program revenues.

Net assets are restricted when constraints placed on them are either externally imposed or are imposed by constitutional provisions or enabling legislation. Internally imposed designations of resources are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, generally it is the Authority's policy to use restricted resources first, and then unrestricted resources as they are needed.

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

As a general rule, the effect of inter-fund activity has been eliminated from the government-wide financial statements.

Measurement Focus, Basis of Accounting and Financial Statement Presentation

Government-Wide Financial Statements – The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the grantor have been met.

Governmental Fund Financial Statements – The Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Authority considers revenues to be available if they are collected within 60 days of the end of the current fiscal year end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

An exception to the "60 day" rule is the recognition of certain patient fee revenues and the related receivables. The Authority has elected to recognize these revenues on the accrual basis of accounting. The difference between the accrual basis of accounting and modified accrual basis of accounting for these revenues is not material to the financial statements.

Expenditures are recorded when the related fund liability is incurred. Exceptions to this general rule include:

- Employees' vested annual leave is recorded as expenditures when utilized. The amount of accumulated annual leave unpaid at September 30, 2005, has been reported only in the government-wide financial statements.
- Interest on general long-term obligations is recognized when paid.
- Debt service expenditures and claims and judgments are recorded only when payment is due.

Bay-Arenac Behavioral Health

Notes to Financial Statements

September 30, 2005

Proprietary Fund Financial Statements – The financial statements of the proprietary funds are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide statements described above.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. The principal operating revenues of the internal service fund are charges to other funds for insurance services. Operating expenses for internal service funds include the cost of claims, administration and reinsurance. Any revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Fund Accounting

The financial activities of the Authority are recorded in individual funds, each of which is deemed to be a separate accounting entity. The Authority uses fund accounting to report on its financial position and results of operations. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts.

The financial activities of the Authority that are reported in the accompanying financial statements have been classified into the following major governmental and proprietary funds.

Governmental Funds

General Fund – This fund account is the Authority's primary operating fund. It accounts for all financial resources of the Authority, except those required to be accounted for in other funds.

Proprietary Funds

Internal Service Fund – This fund represents amounts restricted for risk management which have been set aside to fund the net uninsured exposure of potential shortfalls of Michigan Department of Community Health risk contract revenues.

Budgetary Data

The Authority's general fund budget is under formal budgetary control and follows both the Authority's and Michigan Department of Community Health's annual budget process in establishing the budgetary data presented in the financial statements. The annual fiscal budget is adopted on a basis consistent with accounting principles generally accepted in the United States of America and the requirements of the Michigan Department of Community Health. All appropriations lapse at year end.

Cash and Cash Equivalents

The Authority's cash and cash equivalents are considered to be cash on hand, money market funds, demand deposits and/or certificates of deposit.

A specific amount of cash has been restricted for future payments of compensated absences, depreciation reserve and risk management reserve.

Bay-Arenac Behavioral Health
Notes to Financial Statements
September 30, 2005

Receivables

Accounts receivable in all funds report amounts that have arisen in the ordinary course of business and are stated net of allowances for uncollectible amounts.

Due from other governmental entities consist primarily of amounts due from the Michigan Department of Community Health and affiliates.

Inventories

The Authority does not recognize as an asset inventories of supplies. The cost of these supplies is considered immaterial to the financial statements and the quantities are not prone to wide fluctuation from year to year. The costs of such supplies are expensed when purchased.

Prepaid Items

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

Capital Assets

Capital assets, which include property, plant and equipment, are reported in the government-wide financial statements. Capital assets are defined by the government as individual assets with an initial cost equal to or more than \$5,000 for acquisitions on or after October 1, 2002 and \$500 for acquisitions before October 1, 2002 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if actual cost is not available. Donated capital assets are recorded at estimated fair value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. The Authority does not have infrastructure type assets.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during construction of capital assets is not capitalized. No interest expense was incurred during the current year.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements.

Capital assets of the Authority are depreciated using the straight-line method over the following estimated useful lives:

Assets	Years
Equipment and furnishings	5
Computers	5
Vehicles	5
Leasehold improvements	7-30

Bay-Arenac Behavioral Health
Notes to Financial Statements
September 30, 2005

Incurred but not Reported Claims Liability

The amounts recorded in current liabilities include amounts for incurred inpatient, residential and community provider claims liability based on management's estimate. The Authority may not be billed for these until several months after the date of service. Therefore, the liability is not liquidated within the normal 60-day period after year end. Also, the actual cost may vary from the estimated amount for a variety of reasons that include, but are not limited to, retroactive consumer eligibility or cost recovery from other third party payers.

Deferred Revenue

Deferred revenues arise when the authority receives resources before it has a legal claim to them. In subsequent periods, when the revenue recognition criterion is met, or when the Authority has a legal claim to the resources, the liability for deferred revenue is removed from the fund financial statements and government-wide financial statements, and revenue is recognized.

Compensated Absences

Authority policy allows full time employees to accumulate earned time off at various rates, depending on the employees' length of service with the Authority. Governmental fund financial statements record expenditures when employees are paid for these compensated absences. The government-wide financial statements record expenditures and the related liability when these compensated absences are earned by employees.

Governmental Fund – Fund Balance Reserves and Designations

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditure or (2) legally segregated for a specific future use. The reserves for related assets such as prepaid items are examples of the former. Reserves for compensated absences are examples of the latter.

NOTE 2 - STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Excess of Expenditures over Appropriations

During the year ended September 30, 2005, the Authority incurred expenditures in certain budgetary funds which were in excess of the amounts appropriated as shown on page 4-2 of this report.

NOTE 3 - DEPOSITS AND INVESTMENTS

As of September 30, 2005 the Authority had the following investments:

Investment	Maturities	Fair Value	Cost
Commercial paper	10/03/05	<u>\$ 4,433,581</u>	<u>\$ 4,403,101</u>

Interest rate risk – The Authority manages its exposure to declines in fair value by maintaining a weighted average maturity of twelve months or less.

Credit risk – State statutes and the Authority's investment policy authorize the Authority to deposit and invest in the accounts of Federally insured banks, credit unions, and savings and loan associations; bonds, securities and other direct obligations of the United States, or any agency or instrumentality of the United States; United States government or Federal agency

Bay-Arenac Behavioral Health
Notes to Financial Statements
September 30, 2005

obligations repurchase agreements; bankers' acceptance of United States banks; commercial paper rated by two standard rating agencies within the two highest classifications, which mature not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions which are rated investment grade; and mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan. Financial institutions eligible for deposit of public funds must maintain an office in Michigan. As of September 30, 2005, the Authority's investment in commercial paper was rated A-2 by Standards and Poor's, P-2 by Moody's Investor Services and F2 by Fitch.

Concentration of credit risk – The Authority's investment policy requires diversification by security type and institution. With the exception of U.S. Treasury securities and authorized investment pools, no more than one-third of the total investment portfolio will be invested in a single security type or with a single financial institution.

Custodial credit risk – deposits – In the case of deposits, this is the risk that in the event of a bank failure, the District's deposits may not be returned to it. Non-negotiable, non-collateralized certificates, as is the law in the State of Michigan, shall be evidenced by a safekeeping receipt from the issuing bank. As of September 30, 2005 \$ 17,937,284 of the District's bank balance of \$ 18,452,175 was exposed to custodial credit risk because it was uninsured and uncollateralized.

Custodial credit risk – investments – For an investment, this is the risk that, in the event of the failure of the counterparty, the government will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The entire investment of \$4,433,581 is insured.

NOTE 4 - INTERFUND TRANSFERS

The Authority transferred \$ 193,800 of Medicaid dollars from the General Fund (of the Authority) to the Internal Service Fund risk reserve and transferred \$265,149 of General Fund dollars (appropriated by the State of MI to provide indigent care) from the Internal Service Fund risk reserve to the General Fund (of the Authority) during the fiscal year. These transfers are in accordance with the criteria established by the Michigan Department of Community Health to meet expected future risk corridor requirements and to meet current expenditures of the managed care specialty supports and services program contracts.

NOTE 5 - DUE FROM OTHER GOVERNMENTAL UNITS

Due from other governmental units as of September 30, 2005 consists of the following:

State of Michigan - Medicaid	\$ 49,948
State of Michigan - Other	754,194
Other governmental units	<u>287,947</u>
Total	<u>\$ 1,092,089</u>

NOTE 6 - CAPITAL ASSETS

Depreciable capital asset activity for the year ended September 30, 2005 was as follows:

Bay-Arenac Behavioral Health
Notes to Financial Statements
September 30, 2005

	Balance October 1, 2004	Additions	Disposals and Adjustments	Balance September 30, 2005
Other capital assets				
Equipment and furniture	\$ 3,614,560	\$ 333,224	\$ 408,405	\$ 3,539,379
Vehicles	370,848	11,225	43,226	338,847
Leasehold improvements	153,542	16,875	13,615	156,802
Subtotal	4,138,950	361,324	465,246	4,035,028
Accumulated depreciation				
Equipment and furniture	2,938,528	267,640	408,405	2,797,763
Vehicles	316,993	22,201	43,226	295,968
Leasehold improvements	48,247	20,644	13,615	55,276
Subtotal	3,303,768	310,485	465,246	3,149,007
Net capital assets	\$ 835,182	\$ 50,839	\$ -	\$ 886,021

The Authority has established a reserve for capital purposes, otherwise known in the Michigan Mental Health Code as funded depreciation. Amounts funded to this reserve are restricted for purchase, replacement or improvement of capital assets or retirement of debt related to such capital purposes. The reserve was fully funded for depreciation expense. The balance of the reserve as of September 30, 2005 is \$291,848.

NOTE 7 - DUE TO OTHER GOVERNMENTAL UNITS

Due to other governmental units as of September 30, 2005 consist of the following:

State of Michigan - inpatient residential care	\$ 112,940
State of Michigan - cost settlement	41,875
State of Michigan - leases	52,236
State of Michigan - Quality Assurance Assessment Program (QAAP)	627,939
Other CMH Boards - Access Alliance	1,144,037
Total	<u>\$ 1,979,027</u>

NOTE 8 - LONG-TERM DEBT

Long-term debt consists of compensated absences, and the obligation can be summarized as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amount Due Within One Year
Compensated absences	\$ 1,235,084	\$ 191,416	\$ -	\$ 1,426,500	\$ -

The entire vested amount of accrued compensated absences is considered long-term as the amount expended each year is expected to be offset by vacation time earned for the year.

Bay-Arenac Behavioral Health
Notes to Financial Statements
September 30, 2005

NOTE 9 - RISK MANAGEMENT

Michigan Municipal Risk Management Authority (MMRMA)

The Authority participates in the public entity risk pool – Michigan Municipal Risk Management Authority (MMRMA) for auto and general liability, property and vehicle physical damage coverage.

MMRMA, a separate legal entity, is a self-insured association organized under the laws of the State of Michigan to provide self-insurance protection against loss and risk management services to various Michigan governmental entities.

As a member of this pool, the Authority is responsible for paying all losses, including damages, loss adjustment expenses and defense costs, for each occurrence that falls within the member's self-insured retention. If a covered loss exceeds MMRMA's limits, all further payments for such loss are the sole obligation of the Authority. If for any reason, the MMRMA's resources available to pay losses are depleted, the payment of all unpaid losses of the Authority is the sole obligation of the Authority.

MMRMAs coverage limits are \$15,000,000 for liability and \$1,500,000 for vehicle physical damage. There is a \$250 deductible per vehicle for vehicle physical damage and \$250 per occurrence for property and crime.

Travelers Casualty and Surety Company of America

The Authority has crime coverage through the Travelers Casualty and Surety Company of America. The coverage limit is \$4,000,000 with a \$1,000 deductible per occurrence for crime. If a covered loss exceeds the coverage limit, all further payments for such loss are the sole obligation of the Authority.

Managed Care Risk Contracts

The Authority has managed care risk contracts with the State of Michigan for Medicaid Specialty Supports and Services and for State General Fund Formula Funding for priority populations. The Authority self-insures the risk for these contracts with an Internal Service Fund risk reserve. The Authority holds the Medicaid risk contract and reserve for the region; including the service areas of its affiliates. The State General Fund risk contract and reserve covers only the Authority's specific service area. The contracts provide for the use of contract funds to establish the risk reserve that is restricted to meet future risk obligations. Expenditures from the Internal Service Fund risk reserve will occur if, in any one fiscal year, the Authority finds it necessary to expend more than current resources to provide contractually obligated supports and services for eligible individuals.

NOTE 10 - DEFINED BENEFIT PENSION PLAN

Plan Description – The Authority participates in the Bay County Employees' Retirement System (the Plan), a single-employer defined benefit pension plan that covers substantially all of the employees of the Authority. The Plan provides retirement, disability, and death benefits to plan members and their beneficiaries. The Plan does not issue stand-alone financial statements and is included in the financial report of Bay County.

Bay-Arenac Behavioral Health
Notes to Financial Statements
September 30, 2005

Basis of Accounting – The Plan's financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized when due and the employer has made a formal commitment to provide contributions. Benefits and refunds are recognized when due and payable, in accordance with the terms of the Plan. Administrative costs are financed through investment earnings.

Funding Policy/Contributions – The Authority funds normal costs which are based on actuarially determined rates, expressed as percentages of annual covered payroll, and which are sufficient to accumulate assets to pay benefits when due. The provisions of the Plan require the Authority to contribute at an actuarially determined rate. Plan members contribute at a rate of 4 percent of their annual salary. The Authority pays the plan member contributions for the Authority employees, except for union negotiated contracts which pay their own contributions. The contribution requirements of plan members are established and may be amended by the Authority of Commissioners in accordance with County policies, union contracts, and plan provisions.

Classes of Employees – The Plan's membership consists of the following at December 31, 2004, the date of the last actuarial valuation:

	<u>County</u>	<u>Bay-Arenac Behavioral Health</u>
Retirees and beneficiaries receiving benefits	<u>530</u>	<u>19</u>
Terminated plan members entitled to, but not yet receiving, benefits	<u>75</u>	<u>16</u>
Active plan members	<u>1,203</u>	<u>208</u>

Annual Pension Cost – For the year ended September 30, 2005, the contributions to the plan were as follows:

Authority contribution on behalf of employees	\$ 400,688
Employee contribution	21,889

NOTE 11 - EMPLOYMENT BENEFITS

Upon retirement, an eligible retiree and his/her spouse may be provided health insurance based on credited years of service. Each credited year of service equates to a 5% employer paid health insurance premium. Health insurance benefits will not be provided to deferred retirees, but only to those who will be drawing retirement benefits immediately upon retirement from the Authority. The Authority contributed \$1,846,000 to the Bay County Voluntary Employee Benefit Association (VEBA – a retiree health plan), during the year ended September 30, 2005. Contributions that are made by the Authority are discretionary based on the plan. The following table summarized Bay-Arenac Behavioral Health Authority's determination of unfunded accrued liability as of December 31, 2002 based on an actuarial valuation.

Bay-Arenac Behavioral Health
Notes to Financial Statements
September 30, 2005

Accrued Liability:	
Retirees and beneficiaries	\$ 1,111,016
Active members	<u>5,759,241</u>
Total accrued liability	6,870,257
Valuation of assets	<u>1,399,479</u>
Unfunded accrued liability at December 31, 2002	5,470,778
Less:	
Contributions to plan in 2003	1,664,368
Contributions to plan in 2004	1,039,712
Contributions to plan in 2005	<u>1,846,000</u>
Unfunded accrued liability at September 30, 2005	<u><u>\$ 920,698</u></u>

NOTE 12 - CONTINGENT LIABILITIES

Amounts received or receivable from federal, state and other grantor agencies are subject to audit and adjustment by the grantor. Any disallowed amounts, including amounts already collected, may constitute a liability. The amount, if any, of costs that may be disallowed cannot be determined at this time.

The Authority is currently disputing a Michigan Department of Community Health (MDCH) audit disallowance for the audit period fiscal year 2001 and 2002. The MDCH auditors proposed audit adjustments totaling approximately \$2,568,000 in disallowed expenditures. The Authority is awaiting the written audit report at which time they will appeal the proposed audit adjustments to an MDCH administrative law judge. Bay-Arenac Behavioral Health disagrees with the proposed audit adjustments and intends to vigorously contest the adjustments once they are formalized in the written audit report.

NOTE 13 - OPERATING LEASES

Bay-Arenac Behavioral Health has entered into various operating leases for the use of real and personal property. Operating leases do not give rise to property rights or lease obligations, and therefore, the lease agreements are not reflected in the financial statements.

The following is a schedule of future minimum rental payments required under the operating leases that have initial or remaining non-cancelable lease terms as of September 30, 2005:

<u>Year Ending</u> <u>September 30,</u>	<u>Amount</u>
2006	\$ 865,008
2007	677,510
2008	465,924
2009	154,749
2010	105,450
2011-2012	<u>110,253</u>
Total	<u><u>\$ 2,378,894</u></u>

Bay-Arenac Behavioral Health
Notes to Financial Statements
September 30, 2005

Lease expense for the year ended September 30, 2005 was \$840,948. Bay-Arenac Behavioral Health also has 3 additional leases which are operated on a month to month lease. The total payments on these leases are \$2,514 per month.

NOTE 14 – SUBSEQUENT EVENT

On March 9, 2006, the Authority purchased a building for \$735,000. A loan for \$1,535,000 will finance the purchase of the building and anticipated renovations.

Bay-Arenac Behavioral Health
Statement of Revenues, Expenditures and Changes
in Fund Balance - Budget and Actual
General Fund
Year Ended September 30, 2005

	<u>Budgeted Amounts</u>		<u>Actual</u>	<u>Actual Over (Under) Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Revenues				
State grants				
Department of Community Health Contract				
General Fund	\$ 3,872,769	\$ 4,003,966	\$ 4,019,912	\$ 15,946
Adults Benefit Waiver	655,931	470,082	465,960	(4,122)
Substance Abuse	1,926,477	1,922,161	1,922,271	110
Title XX	21,320	21,320	21,320	-
Other state revenues	42,142	90,756	90,582	(174)
Total state grants	<u>6,518,639</u>	<u>6,508,285</u>	<u>6,520,045</u>	<u>11,760</u>
Federal and state grants	<u>365,401</u>	<u>322,168</u>	<u>310,184</u>	<u>(11,984)</u>
Contributions - local units				
County appropriations	722,679	722,679	722,679	-
Affiliate contributions	710,280	710,280	710,280	-
PA 2 liquor tax	490,454	512,156	512,156	-
Total contributions - local units	<u>1,923,413</u>	<u>1,945,115</u>	<u>1,945,115</u>	<u>-</u>
Charges for services				
Medicaid - DCH contract	55,712,400	58,790,033	59,499,819	709,786
Medicaid - other	110,000	109,554	102,784	(6,770)
Medicaid - prior year settlement	-	-	1,112,003	1,112,003
Client and third party pay	49,341	10,461	56,541	46,080
Other earned contract revenue	2,692,955	2,759,400	2,782,010	22,610
Total charges for services	<u>58,564,696</u>	<u>61,669,448</u>	<u>63,553,157</u>	<u>1,883,709</u>
Interest and rents				
Interest	<u>68,560</u>	<u>234,373</u>	<u>239,777</u>	<u>5,404</u>
Other revenues	<u>38,490</u>	<u>53,361</u>	<u>54,428</u>	<u>1,067</u>
Total revenues	<u>67,479,199</u>	<u>70,732,750</u>	<u>72,622,706</u>	<u>1,889,956</u>

Bay-Arenac Behavioral Health
Statement of Revenues, Expenditures and Changes
in Fund Balance - Budget and Actual
General Fund
Year Ended September 30, 2005

	<u>Budgeted Amounts</u>		<u>Actual</u>	<u>Actual Over (Under) Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Expenditures				
Health & Welfare - Mental Health				
Current:				
Personnel costs	\$ 11,710,513	\$ 11,493,143	\$ 13,312,859	\$ 1,819,716
Operating expenditures	55,335,407	54,907,662	57,649,960	2,742,298
Capital outlay	-	-	361,324	361,324
Total expenditures	<u>67,045,920</u>	<u>66,400,805</u>	<u>71,324,143</u>	<u>4,923,338</u>
Revenues over (under) expenditures	<u>433,279</u>	<u>4,331,945</u>	<u>1,298,563</u>	<u>(3,033,382)</u>
Other financing sources (uses)				
Transfers to Internal Service Fund	-	-	71,349	71,349
Net change in fund balance	433,279	4,331,945	1,369,912	(2,962,033)
Fund balance, beginning of year	<u>4,280,502</u>	<u>4,280,502</u>	<u>4,384,733</u>	<u>104,231</u>
Fund balance, end of year	<u>\$ 4,713,781</u>	<u>\$ 8,612,447</u>	<u>\$ 5,754,645</u>	<u>\$ (2,857,802)</u>

Bay Arenac Behavioral Health - Riverhaven Coordinating Agency
Substance Abuse Prevention & Treatment
Schedule of Budgeted, Reported, and Audited Amounts
Year Ended September 30, 2005

<u>Fund Source</u>	<u>Budgeted (FINAL)</u>	<u>Reported (FINAL RER)</u>	<u>Audited Expenditures</u>	<u>Variance (Audited-Reported)</u>	<u>Local Match Funds</u>
A State Agreement					
1 Community Grant	\$1,789,684	\$1,789,684	\$1,789,684	\$0	
2 SDA	0	0	0	0	
3 SIG	131,927	126,723	126,723	0	
4 Methamphetamine	0	0	0	0	
A Subtotal	<u>1,921,611</u>	<u>1,916,407</u>	<u>1,916,407</u>	<u>0</u>	
B Medicaid					
1 Current Year PEPM	1,056,606	1,056,606	1,056,606	0	
2 Reinvestment Savings	0	0	0	0	
B Subtotal	<u>1,056,606</u>	<u>1,056,606</u>	<u>1,056,606</u>	<u>0</u>	
C Adult Benefit Waiver (ABW)					
1 Current Year PEPM	54,243	54,243	54,243	0	
2 Savings	0	0	0	0	
C Subtotal	<u>54,243</u>	<u>54,243</u>	<u>54,243</u>	<u>0</u>	
D MI CHILD					
1 Current Year PEPM	5,938	5,938	5,938	0	
2 Savings	0	0	0	0	
D Subtotal	<u>5,938</u>	<u>5,938</u>	<u>5,938</u>	<u>0</u>	
E Local					
1 Current Year PA2	512,156	512,156	512,156	0	\$512,156
2 PA2 Fund Balance	26,112	26,112	26,112	0	26,112
3 Other Local (R325.4152 excluding subsection (1)(b))	14,761	14,761	14,761	0	14,761
E Subtotal	<u>553,029</u>	<u>553,029</u>	<u>553,029</u>	<u>0</u>	
F Fees & Collections- Subtotal (R325.4151 (1)(d))	<u>65,618</u>	<u>65,618</u>	<u>65,618</u>	<u>0</u>	65,618
G Other Contracts & Sources (Subtotal)	<u>660</u>	<u>660</u>	<u>660</u>	<u>0</u>	
Grand Total of Subtotals A-G	<u>\$3,657,705</u>	<u>\$3,652,501</u>	<u>\$3,652,501</u>	<u>\$0</u>	

Amount Billable to MDCH (Section A audited subtotal)

\$1,916,407

Total MDCH Payments

1,921,611

(Overpayment)/Underpayment

(\$5,204)

Local Match Funds Total

\$618,647

Local Match Requirement [(Grand Total of Audited Expenditures-B-C-D-G) * 10%]

253,505

Local Match (Shortfall)/Excess

\$365,142

Variance Footnotes

(1)

(2)

(3)

Bay-Arenac Behavioral Health - Riverhaven Coordinating Agency
Substance Abuse Prevention & Treatment
Schedule of Expenditures and Funding Sources by Program
Year Ended September 30, 2005

Program	Budgeted (FINAL)	Reported (FINAL RER)	Audited Expenditures				Audited Funding Sources								Variance Audited- Reported	Questioned Cost (Expenditures - Funding)
			Gross Amount	Less Medicaid	Less Fees	Net Amount	State Agreement	SDA	PA2	Other Local	Other Sources	ABW	MI CHILD	Total Funding		
Administration	\$577,309	\$577,309	\$577,309	\$249,140	\$700	\$327,469	\$312,708	\$0	\$0	\$14,761	\$0	\$0	\$0	\$327,469	\$0	\$0
Prevention	614,668	609,299	609,299	0	0	609,299	481,428	0	127,211	0	660	0	0	609,299	0	0
Treatment	2,136,145	2,141,514	2,141,514	717,772	64,918	1,358,824	897,713	0	400,930	0	0	54,243	5,938	1,358,824	0	0
Women's Services	153,878	153,878	153,878	89,694	0	64,184	64,184	0	0	0	0	0	0	64,184	0	0
HIV/EIP Training	43,778	43,778	43,778	0	0	43,778	33,651	0	10,127	0	0	0	0	43,778	0	0
SIG	131,927	126,723	126,723	0	0	126,723	126,723	0	0	0	0	0	0	126,723	0	0
Methamphetamine	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Other	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Totals	\$3,657,705	\$3,652,501	\$3,652,501	\$1,056,606	\$65,618	\$2,530,277	\$1,916,407	\$0	\$538,268	\$14,761	\$660	\$54,243	\$5,938	\$2,530,277	\$0	\$0
							\$1,916,407									

Reconciliation of PA2 Funds:

Beginning Balance	\$424,521
Current Year PA2	512,156
Expenditures	<u>(538,268)</u>
Ending Balance	<u>398,409</u>

Reconciliation of Medicaid Managed Care (PEPM) Funds:

PEPM Payments Received	\$881,148
Medicaid Savings Carried Over	0
Expenditures	<u>(1,056,606)</u>
Medicaid Savings Carryforward	0
Transfer from PIHP	<u>(175,458)</u>

Bay-Arenac Behavioral Health
Supporting Schedule of Personnel Costs
Year Ended September 30, 2005

General Fund

Personnel costs

Salaries and wages	\$ 8,912,137
Fringe benefits	4,369,267
Board per diem	<u>31,455</u>
 Total personnel costs	 <u><u>\$ 13,312,859</u></u>

Bay-Arenac Behavioral Health
Supporting Schedule of Operating Expenditures
Year Ended September 30, 2005

	<u>General Fund</u>
Operating expenditures	
Advertising	\$ 47,640
Communications	266,007
Consumer related	115,465
Contractual services	775,825
Education and training	17,639
Insurance	82,612
License and fees	16,282
Local funds paid to State	1,255,438
Membership and dues	19,054
Postage	41,231
Quality Assurance Assessment Program (QAAP)	627,939
Publications	10,066
Purchased services	226,963
Purchased services, affiliates	95,130
Recruitment	11,533
Rental equipment	16,590
Rental expense - buildings and other	646,366
Rental expense - State leases	205,812
Repairs and maintenance	211,929
Software license maintenance	331,658
Supplies and small equipment purchases	413,578
Transportation and vehicle expense	43,308
Travel and conferences	189,799
Utilities	89,216
Ancillary services - PT, ST, OT, RN, Dietary	1,319,196
Case Management & Supports Coordination	1,159,561
Community Inpatient Services	981,148
Outpatient services	2,585,594
Residential Home Services	9,602,514
Skill Building/Supportive employment	2,061,313
State Inpatient Services	1,299,735
Subcontract costs	32,099,650
Prevention	784,169
	<hr/>
Total operating expenditures	<u><u>\$ 57,649,960</u></u>



3023 Davenport
Saginaw, MI 48602
Phone (989) 793-9830 / (800) 968-0010
Fax (989) 793-0186

**Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on
an Audit of Financial Statements Performed in
Accordance with Government Auditing Standards**

Board of Directors
Bay-Arenac Behavioral Health
Bay City, Michigan

We have audited the financial statements of Bay-Arenac Behavioral Health as of and for the year ended September 30, 2005, and have issued our report thereon dated February 18, 2006. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered Bay-Arenac Behavioral Health's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Bay-Arenac Behavioral Health's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of Bay-Arenac Behavioral Health in a separate letter dated February 18, 2006.

This report is intended solely for the information and use of the Board of Directors, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Yeo & Yeo, P.C.

Saginaw, Michigan
February 18, 2006



Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control over Compliance in Accordance with OMB Circular A-133

Board of Directors
Bay-Arenac Behavioral Health
Saginaw, Michigan

Compliance

We have audited the compliance of Bay-Arenac Behavioral Health with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended September 30, 2005. Bay-Arenac Behavioral Health's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Bay-Arenac Behavioral Health's management. Our responsibility is to express an opinion on Bay-Arenac Behavioral Health's compliance based on our audit.

We conducted our audit of compliance in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Bay-Arenac Behavioral Health's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Bay-Arenac Behavioral Health's compliance with those requirements.

In our opinion, Bay-Arenac Behavioral Health complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2005.

Internal Control over Compliance

The management of Bay-Arenac Behavioral Health is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Bay-Arenac Behavioral Health's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

Schedule of Expenditures of Federal Awards

We have audited the basic financial statements of Bay-Arenac Behavioral Health as of and for the year ended September 30, 2005, and have issued our report thereon dated February 18, 2006. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the general purpose financial statements taken as a whole.

This report is intended solely for the information and use of the Board of Directors, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Yeo & Yeo, P.C.

Saginaw, Michigan
February 18, 2006

Bay-Arenac Behavioral Health
Schedule of Expenditures of Federal Awards
Year Ended September 30, 2005

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Award Amount	Expenditures
Department of Health and Human Services			
Passed through Michigan Department of Community Health			
Block Grant for Prevention and Treatment of			
Substance Abuse	93.959	\$ 1,789,684	\$ 1,789,684
Less State Funding		550,426	<u>550,426</u>
			<u>1,239,258</u>
Passed through Michigan Department of Community Health			
SIG - Bay Area Social Intervention Services	93.243	131,927	<u>131,927</u>
Department of Health and Human Services			
MIA OBAR PASARR	93.778	95,043	95,043
Less State Funding		23,761	<u>23,761</u>
			<u>71,282</u>
Center for Mental Health Services			
Block Grant for Community Mental Health Services 05 B1 MI CMHS	93.958	130,490	<u>108,502</u>
Substance Abuse and Mental Health Administration for			
Mental Health Services			
McKinney Homeless Act	93.150	40,027	40,500
Less State Funding		23,027	<u>23,000</u>
			<u>17,500</u>
Passed through Michigan Family Independence Agency			
Strong Families -- Safe Children	93.556	31,707	<u>31,707</u>
Total Department of Health and Human Services			<u>1,600,176</u>
Housing and Urban Development			
Passed through Michigan Department of Community Health			
Supportive Housing Program	14.235	18,044	17,780
Less State Funding		722	<u>711</u>
			<u>17,069</u>
Total Federal programs			<u><u>\$ 1,617,245</u></u>

Bay-Arenac Behavioral Health
Notes to the Schedule of Expenditures of Federal Awards
September 30, 2005

NOTE 1 - GENERAL

The accompanying Schedule of Expenditures of Federal Awards presents the activity of all federal financial assistance programs of Bay-Arenac Behavioral Health. All federal financial awards passed through other government agencies are included on the schedule.

NOTE 2 - BASIS OF ACCOUNTING

The accompanying Schedule of Expenditures of Federal Awards is presented using the accrual basis of accounting.

NOTE 3 - RELATIONSHIP TO BASIC FINANCIAL STATEMENTS

Federal financial assistance revenue is included in the basic financial statements as federal and state grants.

Bay-Arenac Behavioral Health
Schedule of Findings and Questioned Costs
September 30, 2005

SECTION I - SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified? _____ yes X no
- Reportable condition(s) identified that are not considered to be material weaknesses? _____ yes X none reported

Noncompliance material to financial statements noted? _____ yes X no

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? _____ yes X no
- Reportable condition(s) identified that are not considered to be material weakness(es)? _____ yes X none reported

Type of auditors' report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133? _____ yes X no

Identification of major programs:

CFDA Number(s)

Name of Federal Program or Cluster

93.959

Block Grant for Prevention and Treatment of Substance Abuse

Dollar threshold used to distinguish between type A and type B programs: \$ 300,000

Auditee qualified as low-risk auditee? X yes _____ no

**Bay-Arenac Behavioral Health
Schedule of Findings and Questioned Costs
September 30, 2005
(continued)**

SECTION II - GOVERNMENT AUDITING STANDARDS FINDINGS

There were no findings related to the financial statements which are required to be reported in accordance with generally accepted government auditing standards for the year ended September 30, 2005.

SECTION III - FEDERAL AWARD FINDINGS

There were no findings or questioned costs for Federal Awards for the year ended September 30, 2005.

**Bay-Arenac Behavioral Health
Summary Schedule of Prior Audit Findings
September 30, 2005**

There were no audit findings for the year ended September 30, 2004.



3023 Davenport
Saginaw, MI 48602
Phone (989) 793-9830 / (800) 968-0010
Fax (989) 793-0186

February 18, 2006

Board of Directors
Bay-Arenac Behavioral Health
Bay City, Michigan

In planning and performing our audit of the financial statements of Bay-Arenac Behavioral Health for the year ended September 30, 2005, we considered the Organization's internal control in order to determine our examination procedures for the purpose of expressing an opinion on the financial statements not to provide assurance on the internal control system.

However, during our audit we became aware of certain matters that are opportunities for strengthening internal controls and operating efficiency. The following summarizes our comments and suggestions regarding those matters. This letter does not affect our report dated February 18, 2006, on the financial statements of Bay Arenac Behavioral Health.

BUDGET PROCESS

The budget is an important management tool. It assists to ascertain that: expenditures are within available financial resources; costs relative to importance of programs and activities are periodically reevaluated for present and future needs; internal operations are systematically reexamined for efficiency and economy so that improvements might be made; and data concerning specific areas of responsibility are readily available for evaluative purposes.

The budget is based on past experience and management's intentions or expectations of future conditions that will affect the Authority. The actual reported expenditures exceeded the budget by \$4.9 million. The excess expenditures consist primarily of the VEBA contribution (\$1.8 million), Quality Assurance Assessment Program (QAAP) (\$.6 million), and additional funds to affiliates (\$1.5 million). Although the expenditures were authorized, they were not part of the budget. We recommend that the Authority incorporate all expenditures into the budget. This will assist the Authority to comply with the Uniform Budget Act, Public Act 621 of 1978 and controlling expenditures and cash flow.

Management's Response:

BABHA develops an operating budget, monitors and amends the budget as necessary with Board approval. Variances are consistently monitored. During the year in question, the board approved expenditures without a budget amendment because the exact amount of the commitment could not be precisely predicted at the time the commitment was made. In the future, a budget amendment will be made using the best estimate available at that point in time.

STATUS OF PRIOR YEAR COMMENTS:

We have reviewed the status of comments and recommendations made in the prior year. The status of prior year comments is as follows:

Comment	Implemented/ Situation Corrected	Progress Made	Situation Still Exists
Modify capital asset policy to consider leasehold improvements under operating leases that are shorter than the policy for useful lives	X		
Monitor journal entries	X		
Restrict access to payroll accounting system	X		

This report is intended solely for the information and use of the board of directors, management and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

We will review the status of these comments during our next audit engagement. We have already discussed the comments and suggestions with various personnel, and we will be pleased to discuss them in further detail at your convenience, to assist you in implementing the recommendation.

Very Truly Yours

Yeo & Yeo, P.C.
CPAs and Business Consultants



Mari McKenzie